My Focus Is on the Role and Structure of Governments

• Not on the nation-state
  – There’s a rapidly growing economics literature there
• Rather, on local governments
• They’re important
  – There are 90,000 in the United States
  – Their share of GNP is growing faster than the national government’s share
• But the role and structure of governments has been much neglected by scholarship in law, economics, and political science
• I’ll just focus on some broad issues
Governments Are Generally Viewed as Distinct from Private Firms

• In contrast, I’ll try to offer a common framework
  – Rooted in institutional economics
  – Focused on U.S. institutions
  – But analysis is general
  – Comparison with other countries raises important questions

• I won’t make many references to the literature
We Must Begin with a Definition of “Government”

• There is evidently no standard definition
  – We have to provide one

• A (classical, or territorial) government is:
  – A legal entity
  – Associated with a defined territory
  – With the authority to provide services to residents of the territory
  – And the authority to require payment for the services from the residents
Some Elaboration

• Payment may be extracted through:
  – General taxes (on, e.g., property, sales, or income)
  – Assessments calculated according to estimated benefits received
  – User fees

• A resident must leave the territory to escape liability for assessments

• Nearly all governments are regulated by higher-level governments, as with private organizations
Control

• Governments can be:
  – Autocratic (directors are self-perpetuating)
  – Hierarchical (directors are appointed by a higher-level government)
  – Democratic (directors are elected by residents)

• I’ll focus primarily on:
  – Democratic governments
  – In the United States
“Government,” not “The State”

• Weber: state holds “the monopoly of the legitimate use of physical force within a given territory.”

• But most governments have no guns (and nearly none did before 1840)

• Rather, most governments compel payment of assessments the same way a merchant compels payment of purchase prices:
  – By bringing a lawsuit
Governments Differ from Private Enterprise Principally in Formation

• Can be formed by higher government and/or vote of local residents

• Either way, all residents of designated territory become members of the government
  – Must pay assessments

• Condominium apartment building or rural electricity cooperative can’t do that
  – Though the latter can come very close

• After formation, governments and private firms are very similar
  – Majority vote of members controls
Governments Provide Territorially Monopolistic Services

• Such as roads, sewage systems, mosquito abatement, traffic regulation, zoning, courts to decide disputes involving externalities

• Don’t operate in Tiebout’s world: residents face relatively high costs of moving
  – E.g., because of territory-specific investments in employment, housing, friends, schools, etc.
Don’t Generally Produce:

• Public goods, such as radio or TV broadcasting
  – Generally privately provided

• Goods whose quantity or quality is difficult for customers to assess
  – E.g. medical care, nursing care, or child care
  – These are generally provided by nonprofits where proprietary firms are inadequate
Governments Are Essentially Territorial Cooperatives

- Democratic governments provide customer ownership of monopoly services
- Just like private cooperatives
- There’s much overlap between services provided by coops and those provided (or regulated) by local governments:
  - E.g., electricity, telephone, water
- Other private organizations are even closer to governments:
  - Residential condominiums
  - Homeowners’ associations
  - Planned communities
Costs of Voting

• Private coops reflect a strong tradeoff between:
  – Costs of monopoly
  – Costs of collective decision-making when interests of voters are heterogeneous

• Evidence suggests latter are often high
  – Costly procedures (getting information, organizing)
  – Bad decisions (uninformed, exploitative)

• Coops – indeed all firms with multiple owners – generally survive only where customer-owners are, or can be made to be, highly homogeneous in their interests in the firm
  – E.g., corn farmers, hardware retailers, taxi drivers, lawyers
  – And shareholders in business corporations
The Same Should Be True of Governments

• Survivorship should (roughly) select for efficiency in governmental structures

• Governments should adopt strategies to homogenize interests of resident-voters
  – E.g., boundaries of territory

• So we can look at organizational trends for evidence of comparative costs and benefits of alternative structures
Consider Number of Purposes

• The 2012 U.S. Census of Governments counts roughly 90,000 “governmental units”
  – 40,000 general-purpose governments (“GPGs”)
    • Counties
    • Municipalities
    • Townships
  – 50,000 special-purpose governments (“SPGs”)
    • 13,000 school districts
      – We’ll ignore these until later
    • 37,000 “special” districts
      – We’ll focus particularly on these
Special Purpose Governments

• Also called “special districts” or “special assessment districts”

• Pursue a single purpose – providing one or another of the same services provided by GPGs
  – E.g. sewage, electricity, sidewalks, street lighting, parks, irrigation, mosquito abatement, road maintenance, fire protection, hospitals

• Have attributes similar to GPGs, but provide a single service

• Formed by private initiative with majority vote of residents of proposed territory

• Governed by state enabling statutes

• Increasing rapidly in economic importance
Fundamental Question

• Why just single-purpose or general-purpose governments?
  – Why no two-purpose or three-purpose governments?
  – Law isn’t the constraining factor

• Proposed answer: These are the two best strategies for limiting costs of collective decision-making
Single-Purpose Solution to Homogeneity of Electorate

• E.g., irrigation district for a watershed
  – Members are landowners
  – Assessments and votes are based on benefits – e.g. acres in agricultural production

• Induces single-peaked preferences
  – Principal concern is aggregate water flow

• Adding a second purpose – e.g., electricity distribution or fire protection – would allow customers of one service to exert monopoly power over the other

• Adding a third service could result in no stable coalition at all
Many-Purpose Solution to Homogeneity of Electorate

• A government for every service involves much redundancy

• The most workable alternative to multiple SPGs is apparently at the other extreme:
  – Bundle together in one organization as many services as possible

• As the number of services increases:
  – Ability and incentive to form a stable exploitative coalition of residents decreases
  – Homogeneity of interest in package as a whole increases

• Presses residents toward a common interest in efficient management of all services in a general bundle

• Explains why a given territory rarely has more than one GPG, though it may have many SPGs.
City Manager Model Goes Further

• City council members elected at large
  – Strongly homogenizes voting outcomes
• Council hires professional manager
• Model is a product of the Progressive Era
  – Has been slowly but steadily spreading since
• There’s reason for skepticism about recent proposals to increase partisanship in local elections
Constitutional Voting Rights

• U.S. Supreme Court has extended a one-person-one-vote rule to all GPGs.
• But not to SPGs, except for school districts.
• Court says the criterion is whether the entity provides "governmental" services.
  – Silly: SPGs and GPGs provide the same services.
• Rather, it’s easy -- and necessary -- to treat SPGs differently from GPGs because they’re polar solutions to the voting problem:
  – So there’s no ambiguity in regulating their voting rights differently.
  – Voting proportional to interest is key in SPGs, not GPGs
Hybrid Structures

• Increasingly, municipalities are spinning off individual services to SPGs serving the same territory
  – Presumably homogenizes voting while maintaining some economies of scope
  – Presumably most useful when service is a major part of budget
    • Like primary and secondary education
    • Would unbalance homogeneity of interest in general SPG service package
More on School Districts

• Very heterogeneous demand
  – Voting by residents may provide too little (or too much)
  – Funding with general taxes tends to subsidize families with children

• So formation of districts is compelled by state
  – Also one-person-one-vote
  – And taxation is regulated and subsidized by state
Free Formation of Governments?

• Initially, states adopted a separate enabling statute for each different type of SPG
  – And required approval by state official
• Current tendency is toward:
  – A single general enabling statute
  – No ex ante approval
• Same evolutionary pattern as:
  – Business (joint stock) corporations
  – Cooperative corporations
  – Nonprofit corporations
• A general solution to the problem of collective action (Olson, Ostrom)?
Toward Governmental Fragmentation?

• Economies of scale in territorial defense now far exceed those for most other governmental services

• And other services can be provided by specialized governments that have different territories

• Perhaps this is what a post-Westphalian world, without nation-states, will look like
Why So Few SPGs in Other Countries?

- Largely a U.S. phenomenon
- Switzerland uses them
- And Bruno Frey, almost uniquely, has studied them
Non-Territorial Governments

• Have long existed for trades pursued by individuals:
  – Guilds
  – Bar associations
  – Trade unions

• Self-regulatory and standard-setting organizations (SROs and SSOs) are now extremely important
  – Have firms as members
  – Generally voluntary
  – But have de facto monopoly
  – And sometimes have governmental authority

• Should SROs be permitted to form as governments?
  – As of right?
  – Can antitrust problems be dealt with separately, as with business corporations?
Conclusion

• Governments are closer to private enterprise than conventional discourse suggests
• Simple analytic tools taken from the analysis of private enterprise can help illuminate the role and structure of “public” enterprise as well